

DECISION

**THE COMPTROLLER GENERAL
OF THE UNITED STATES**
WASHINGTON, D. C. 20548

File
2427

FILE: B-208281

DATE: February 16, 1983

MATTER OF: Varian Associates, Inc.

DIGEST:

Exercise of a contract option by the contracting agency following agreement by the awardee to significantly reduce the contract option price amounted to negotiations on a sole-source basis with the awardee for the additional items needed by the agency. Where the facts indicate that price competition was available for the additional items, agency was not justified in negotiating solely with the contractor for these items.

Varian Associates, Inc. (Varian), protests the award to International Telephone and Telegraph Corporation (ITT), Electron Tube Division, of a 100-percent option to the contract awarded to ITT under request for proposal (RFP) DAA09-82-R-5525 issued by the United States Army Armament Materiel Readiness Command, Rock Island, Illinois. The RFP had called for the supply of 235 Power Amplifier Klystron Tubes.

Varian contends that because it informed the contracting officer in writing prior to the exercise of the option that it would be willing to offer on any add-on quantity a price less than ITT's winning offer under the RFP, the Army's exercise of the option clause of ITT's contract was unreasonable and in violation of the option exercise requirements of Defense Acquisition Regulation (DAR) § 1-1505 (1976 ed.).

For the reasons set forth below, we sustain Varian's protest.

The RFP was issued on January 8, 1982, and provided for a first article testing requirement and 100-percent option. Two price proposals were received in response to the RFP at the following unit prices:

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<u>Offeror</u>	<u>With First Article</u>	<u>Without First Article</u>	<u>Option</u>
ITT	\$3,280	\$3,280	\$3,590
Varian	\$3,365	\$3,325	\$3,547

The Army awarded a contract on May 25, 1982, to ITT at a unit price of \$3,280. The options were not evaluated.

On May 28, 1982, the Army found that it needed an additional 188 Klystron Tubes. In response to a request from the Army, ITT offered to reduce its option price to \$3,280 and to change the F.O.B. origin method of shipment specified in the contract option clause to F.O.B. destination if the Army would increase the quantity to 235, or the full 100-percent option quantity.

On the basis that the unit price agreed to by ITT would be the same as the original contract price and that a better price would not likely be obtained by advertising the additional requirement, the contracting officer recommended on June 18, 1982, that the exercise of the option was in the best interest of the Government. However, on July 13, 1982, Varian hand-delivered a letter to the contracting officer which stated:

"Please be advised that on the subject procurement, Varian's Microwave Tube Division is now prepared to offer a more attractive price for your follow-on requirements. Specifically, Varian is prepared to offer a price less than the winning bidder's price of \$3,280.00 each for a similar quantity of the referenced part number.

"We trust that this advice will constitute a clear indication that a better price can be obtained by a new solicitation than by exercise of the current contract option. * * *"

The contracting officer took no action on Varian's letter. The option clause of ITT's contract was, instead, exercised on July 14, 1982, by a modification to ITT's contract. The RFP modification provided that delivery of the additional 235 tubes would begin on June 30, 1983, and run through March 31, 1984.

Varian asserts that because its July 13, 1982, letter provided a clear indication that a new solicitation for additional tubes would result in a price lower than ITT's award price, the Army's exercise of the option clause of ITT's contract was inconsistent with DAR § 1-1505 (1976 ed.). More specifically, Varian argues that the Army failed to comply with DAR § 1-1505(d)(2) (1976) which provides that before an option can be exercised an informal investigation of prices, or other examination of the market, must clearly indicate that a better price than that offered by the option cannot be obtained. According to Varian, the Army not only did not conduct an informal investigation of prices, but also chose to ignore Varian's intention to offer a lower price on any subsequent competition without inquiring of Varian the exact price the company intended to offer.

In addition, Varian questions the delivery schedule for the additional quantity award to ITT. Varian claims a delivery schedule beginning in June of 1983 and ending March of 1984 does not seem to be in accordance with DAR § 1-1505(c)(iii) (1976) which states that the exercise of a contract option be the most advantageous method of fulfilling the Government's need. In this regard, Varian alleges that a new solicitation for the additional quantity could have provided for deliveries of Klystron Tubes that were simultaneous with the delivery schedule for the original 235 units. Varian further alleges that given a normal leadtime for a new solicitation, an award under such a solicitation could have been made in August 1982. Thus, Varian argues that the Army would have lost only 30 calendar days if it had issued a new solicitation for the additional quantity.

The Army states the RFP had requested an option exercise period of 120 days from the date of award but ITT specified in its proposal that the option would expire on

July 23, 1982. The Army further states that it considered the close proximity of the option exercise period to the competition on the basic contract quantity and the \$3,280 per unit option price offered by ITT and concluded that a new solicitation would not produce a lower price than that available from ITT. As to the time required to complete a new procurement, the Army declares that the 6 to 9 weeks for receipt of a solicitation technical data package and issuance of a new solicitation, and the 16 to 18 weeks for evaluation of proposals and award of contract would have exceeded the time during which ITT's option could have been exercised. Finally, the Army states that the need for continuity of production, the excellent performance record of ITT, and the administrative cost in time and money also influenced the decision to exercise the option clause of ITT's contract.

With regard to the Army's conclusion that little change in prices had occurred prior to the exercise of the option, Varian claims that such a conclusion might be consistent in a competitive commercial market but is completely inconsistent for a two company industry with essentially the Government as its only customer.

While both Varian and the agency have framed the issue before our Office as the propriety of the exercise of an option, we do not view that as the initial issue.

The option price in the contract awarded to ITT was \$3,590 per unit. Varian advised that it would offer a price less than \$3,280 per unit, over \$300 less than ITT's option. Only because the contracting officer had negotiated a reduction in ITT's contract option price was ITT's price determined the best price available at the time.

Basically, an option is an unaccepted offer to sell upon agreed terms which may be unilaterally accepted by the Government. 1 Comp. Gen. 752 (1922) and DAR § 1-1501 (1976). An option should be clear and definite and should not require further negotiations to work out important and essential terms. Department of Health and Human Services - Reconsideration, B-198911.3, October 6, 1981, 81-2 CPD 279. Therefore, the essential terms of an option and the

corresponding commitment on the part of the contractor have to be established at the time the underlying contract is awarded. If they are not, there is no option for exercise by the Government. Department of Health and Human Services - Reconsideration, supra.

The terms of the RFP's option clause were clear and specific as to the price at which the option was to be exercised. Paragraph H.4 of the RFP's Special Provisions provided as follows:

"The Government may increase the quantity of the supplies called for herein, not to exceed the percentage in section B and at the unit price set forth below. The Contracting Officer may exercise this option at the unit price set forth below. The Contracting Officer may exercise this option at any time preceding One Hundred Twenty (120) days after award of contract by giving written notice to the contractor. Delivery of the items added by the exercise of this option shall continue immediately after, and at the same rate as, delivery of the items called for under this contract unless the parties otherwise agree.
* * *

In view of the regulatory requirements for the exercise of a contract option and in view of the language of the RFP requiring the option to be exercised at the offeror's stated option price, we find that the contracting officer's actions here were inconsistent with the unilateral exercise of a contract option. Rather, we conclude that what the contracting officer did instead was conduct negotiations for the needed tubes and award a contract on a noncompetitive basis. The issue thus presented is whether an adequate justification existed for such an award.

As a general matter, Government procurements must be conducted on a competitive basis to the maximum extent practicable. DAR § 3-210 (1976 ed.). A sole-source acquisition may be authorized, however, where the procuring

agency's minimum needs can be met only by items or services that are unique; time is of the essence and only one known source can meet the agency's needs within the required timeframe; a sole-source award is necessary to insure compatibility between the procured item and existing equipment; or an award to other than the proposed sole-source contractor would pose unacceptable technical risks. Cereberonics, Inc., B-205063, April 14, 1982, 82-1 CPD 345.

None of the above justifications are present here. In making the decision to exercise ITT's option, it appears that the contracting officer relied primarily on the fact that the time between the award of the contract containing the option was so short that it indicated that ITT's reduced option price of \$3,280 per unit was the lowest price obtainable. See DAR § 1-1505(d)(3) (1976). The record shows that the need for continuity of production, the excellent performance record of ITT, and the administrative cost in time and money of resolicitation also influenced the contracting officer in his decision to exercise ITT's option.

Regarding the use of price as the justification, even for the proper exercise of an option, which we find was not done here, the Army's reliance on our decision in A. J. Fowler Corporation, B-205062, June 15, 1982, 82-1 CPD 582, is misplaced.

The Army argues that a mere assertion of a lower price by a protester does not provide any basis for questioning the determination to exercise an option provided that the determination was reasonable under the circumstances it was made. In, A. J. Fowler, *supra*, we stated that the protester "is not necessarily entitled to a second chance merely by guaranteeing to offer a lower, but unspecified, price--particularly since there is no indication that it would result in more than minimal savings to the Government."

The issue in that decision was whether the agency was required to test the market by resoliciting for its requirements rather than by an informal investigation of prices. The protester argued that under DAR § 1-1505(d)(1) (1976), the agency's requirements had to be resolicited because of the protester's "guarantee" in its protest that it would perform at prices lower than the option prices in the two contracts under which the options were exercised. We noted with respect to one contract that the protester did not file its protest containing the lower price guarantee until after the option had already been exercised by the contracting officer.

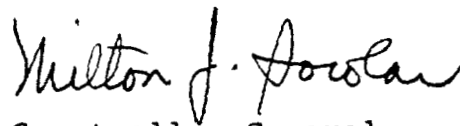
However, as to the other contract, where the guarantee came in prior to the exercise of the option, we concluded that the agency was not required to test the market through a resolicitation because the option price had already been tested by a competition, because the prices were evaluated in the initial award selection, in which the protester had a full opportunity to participate. Here, the option prices were not evaluated and further unjustified negotiations were conducted with ITT.

Protest sustained.

We recommend that the contract awarded to ITT for the additional 235 Klystron Tubes be terminated for the convenience of the Government and the requirement be competitively solicited. We note that the Army emphasizes the urgency of the requirement and that resolicitation will take additional time for the issuance of a new solicitation and for evaluation and award. However, under the contract modification for the additional tubes delivery is not to begin until 1 month after completion of all deliveries under the awarded contract, June 30, 1983. Moreover, the Army's need at the time it increased ITT's contract quantity by 235 was only for 188 Klystron Tubes. In view of the fact that a technical data package was developed for the RFP under which ITT was awarded the original contract quantity, we see no reason why a contract under a competitive solicitation for the additional quantity cannot be awarded by June 1983.

We recognize that additional time after award would be needed for approval of first article before any deliveries can take place. In this regard, the Army informs us that ITT obtained first article approval for its product on November 30, 1982. With respect to first article approval for Varian's product, in the event the company should win the award, we note that ITT's delivery schedule under the existing contract modification for the additional 235 Klystron Tubes calls for delivery of only 75 of these tubes by the end of August 1983. We think that the Army should allow Varian the opportunity to propose the shortest time possible for the submission of its product for first article testing. Finally, in a competitive solicitation for the additional tubes, the Army, in our opinion, would have a great deal of flexibility in negotiating the type of delivery schedule it needed to fulfill its requirements.

This decision contains a recommendation for corrective action to be taken. Therefore, we are furnishing copies to the Senate Committees on Governmental Affairs and Appropriations and the House Committees on Government Operations and Appropriations in accordance with section 236 of the Legislative Reorganization Act of 1970, 31 U.S.C. § 720 (formerly 31 U.S.C. § 1176 (1976)), which requires the submission of written statements by the agency to the committees concerning the action taken with respect to our recommendation.

for 
Comptroller General
of the United States